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More Cash Balance Plan Sponsors Choosing Actual Rate of Return in the Wake of IRS Approvals and Pending Regulations

As of January 2014, 30% of Kravitz clients with large Cash Balance plans (more than 100 participants) have adopted Actual Rate of Return as the Interest Crediting Rate (ICR), while others are exploring the advantages. Kravitz has received many IRS favorable determination letters for these plans since new IRS regulations were issued in 2010, and final regulations are pending. For plan sponsors seeking greater flexibility and reduced investment risk, Actual Rate of Return is an increasingly popular choice.

Background: Understanding “Actual Rate of Return”

Every Cash Balance plan has a guaranteed Interest Crediting Rate (ICR) written into the plan document. Plan participants must receive an annual employer contribution plus an interest credit based on the ICR. Prior to the 2010 IRS regulations, most plans used conservative safe harbor rates such as the 30-year Treasury rate. The 2010 regulations broadened investment options, allowing plan sponsors to set the ICR to equal what the plan investments actually earn in the market (the “Actual Rate of Return”), rather than trying to target a specific rate of return each year. The employer’s investment risk is reduced considerably, and participants are protected by various investment rules, including preservation of capital.

Key Advantages of Choosing an Actual Rate of Return ICR:

- Removes most of the challenges of exceeding or falling short of a targeted ICR every year
- Allows for predictable annual contributions
- Options for strategically managing market volatility by setting a cap on the ICR

How Kravitz Can Help:

Kravitz has already assisted many clients in setting up Actual Rate of Return plans, and has worked with others to convert from a traditional safe harbor rate to Actual Rate of Return. This option is typically best suited for larger plans, since in smaller plans the fluctuation in market returns may impact staff contributions. Your Kravitz consultant can review your plan with you and help determine the optimal choice of ICR. We offer the following services to all of our clients:

- ✓ Consultation and analysis to determine whether Actual Rate of Return is an appropriate choice for meeting the plan sponsor's goals
- ✓ Expert guidance in setting up and managing a new Actual Rate of Return plan
- ✓ Seamless conversion of an existing plan from a safe harbor rate to Actual Rate of Return
- ✓ Obtaining IRS Favorable Determination Letters

Proven Success:

- 30% of Kravitz Cash Balance clients with more than 100 participants are currently using Actual Rate of Return
- Kravitz Actual Rate of Return plans cover over 2,400 participants and over \$220 million in assets
- IRS approval: Kravitz has already obtained Favorable Determination Letters for many Actual Rate of Return Cash Balance plans

Coming Soon – New Guidance from the IRS

We are anticipating new in-depth IRS guidance on Actual Rate of Return plans early in 2014, which will ensure that these plans run even more smoothly. Our actuarial team includes legislative experts standing by to analyze these regulatory changes, helping our clients take advantage of the new rules while remaining in full compliance with IRS rules.

What Should Plan Sponsors Do Now?

If you are interested in exploring Actual Rate of Return for your plan, please contact your Kravitz consultant. We will continue to communicate with you regularly regarding the implications of the new and proposed Cash Balance regulations and their impact on managing plan investments.

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